



INDONESIA: ECONOMIC AND FINANCIAL HIGHLIGHTS MARCH 2005

Summary:

- March 1 fuel price hikes drove year-on-year (YoY) inflation to 8.8% in March 2005, its highest level since January 2003.
- The rupiah declined 1.7% against the dollar in March.
- The GOI postponed dollar and domestic rupiah bond auctions despite high demand, judging borrowing costs as too high.
- Bank Indonesia (BI) is setting up a credit bureau to consolidate and report data on borrowers.
- Parliament has agreed to budget emergency funds for disaster areas in Aceh province.
- The Jakarta Stock Exchange index rose in March but the GOI postponed its divestment of Bank Central Asia shares.
- Philip Morris acquired 40% of Indonesian cigarette manufacturer Sampoerna in one of the largest foreign investments in Indonesia in several years.
- The Supreme Audit Board (BPK) found irregularities involving the budgets of the Ministry of Defense, the Army and the Ministry of Culture and Tourism in its report to Parliament for the second half of 2004.
- Through March 2005, Indonesia's Financial Intelligence Unit (PPATK) had received 1,549 suspicious transaction reports from financial institutions.

Fuel Price Increases Drive Inflation Higher

On April 1, the Central Statistics Bureau announced YoY Consumer Price Inflation (CPI) of 8.8%, largely due to fuel price increases from the March 1 fuel subsidy cut. Month-on-month inflation rose 1.91%. This is the highest monthly inflation rate since January 2003.

On March 4, the GOI established an interagency team to monitor inflation and make recommendations for monetary and fiscal policy in the wake of the March 1 fuel price hike. BI Head of Public Relations Erwin Riyanto stated that BI would gradually increase interest rates over the course of the calendar year to maintain inflation at or below 7%.

Rupiah Depreciates in March

The rupiah declined by 1.73% against the USD during March 2005, settling at Rp 9,480/USD on March 31. In addition to higher than expected inflation figures, analysts also attributed the rupiah's fall to strong corporate dollar demand. Companies tend to buy

dollars at the end of each quarter to repay maturing debt. State-owned oil company Pertamina alone purchases an average of USD 30-40 million per day, which can escalate to USD 200 million daily as the end of a quarter approaches. Analysts believe BI intervened on a number of occasions in March 2005 to reduce rupiah/USD volatility.

GOI Cuts Fuel Subsidy, Submits Revised Budget

The GOI cut fuel subsidies effective March 1, resulting in fuel price increases of 29% on average. In 2004, fuel subsidies cost the GOI approximately Rp 61 trillion or USD 6.6 billion, more than four times the budgeted amount. The price of premium gasoline rose by 33% to Rp 2,400 (USD 0.25) a liter, and the cost of automotive and industrial diesel increased by 27% and 33% respectively. Prices for other types of fuel also rose. The price for household kerosene, widely used for cooking by lower income families, was left unchanged. Economists expect higher fuel prices to lead to increased manufacturing and transportation costs, which in turn will likely lead to higher prices for some basic goods. The GOI has said it will cap transportation price increases at 10%.

On March 8, the government announced it would submit revisions to the 2005 budget to reflect the reduction of fuel subsidies and Rp 10.5 trillion (USD 1.13 billion) in compensation programs for the poor. On March 23, the Ministry of Finance (MOF) submitted a draft revised budget to Parliament. The GOI has promised to re-direct fuel subsidy savings to education, health, infrastructure, and rice subsidy programs for the poor. The GOI also budgeted Rp 5.6 trillion (USD 588 million) for 9.7 million scholarships for low-income students. Another Rp 18.1 trillion (USD 1.9 billion) is planned for anti-poverty programs, of which Rp 10.5 trillion (USD 1.1 billion) will come from fuel subsidy savings. Regulation No. 17/2003 requires the GOI to submit a revised budget to Parliament before the end of June each year.

DPR Agrees on Aceh Funds, Rejects Presidential Decree

On March 23, Parliament agreed to use emergency funds of RP 1.26 trillion (USD 132 million) for areas damaged by the December 26, 2004 tsunami. The 2005 budget had already allocated Rp 2 trillion (USD 210 million) in emergency funds. In its March 26 Aceh Reconstruction Master Plan, the State Ministry for National Development Planning (BAPPENAS) estimated funds required for rehabilitation and reconstruction in tsunami-affected areas at approximately RP 57 trillion (USD 6 billion). (NOTE: This does not include estimates for the more recent March 28, 2005 earthquake.)

During a March 1 hearing, Parliamentary Commission VI (trade, industry, investment, cooperatives, state-owned enterprises and small-to-medium enterprises) rejected Presidential Decree No. 9/2005 concerning the "Position, Function, Governance, and Organizational Structure of the Ministry for Cooperatives and Small-to-Medium Enterprises" (SMEs). The decree would have eliminated the Ministry's technical (but not administrative) authority and was viewed by Parliament as in conflict with regulation UU

No. 36/2004 concerning the 2005 budget. Parliament's rejection makes it difficult for the GOI to proceed with five planned programs: (i) development of 7,000 cooperative units to serve 2 million members; (ii) enhancement business climate for cooperatives, micro-businesses and SMEs (KUMKM); (iii) financing facility for KUMKM; (iv) development of 6 million new SMEs (especially IT-based); (v) development of KUMKM into business clusters. The Ministry for Cooperatives and SMEs is currently preparing an amendment to the decree and plans to re-submit to Parliament later this year.

Banking Sector Update

On March 5, Indonesian bankers signed the "Nusa Dua Declaration" (named after a hotel complex in Bali) confirming their support for BI's bank consolidation initiative. There are currently 134 banks in Indonesia. The top ten banks hold approximately 63% of all loans. BI wants the 52 smallest banks with capital under RP 100 billion (USD 11 million) to merge with larger anchor banks, the criteria for which BI plans to announce in June. Bank Rakyat Indonesia (BRI) and Bank Negara Indonesia (BNI) have submitted a proposal to merge with Bank Tabungan Negara (BTN) to the government.

The following is a list of Indonesia's 10 largest commercial banks by value of outstanding loans:

Banks	Total loans (Rp trillions)	Market share (%)
Bank Mandiri Tbk *	88.2	15.8
Bank Rakyat Indonesia *	61.5	11.0
Bank Negara Indonesia *	58.8	10.5
Bank Central Asia	42.3	7.2
Bank Danamon Indonesia	29.2	5.2
Bank Niaga	21.3	3.8
Bank Permata	14.8	2.6
Bank Bukopin	13.0	2.3
Bank Internasional Indonesia	12.9	2.3
Bank Tabungan Negara *	12.6	2.2

Source: Bank Indonesia

** State-owned*

Government and Corporate Bond Market Update

Citing unfavorable market conditions and a rising interest rate environment, on March 24 Indonesia postponed planned dollar and rupiah-denominated bond issuances until further notice. Indonesian sovereign international bonds have been rated B plus by Standard and Poor's.

The corporate bond market continued to perform well despite threats of rising interest rates. The GOI approved Bank Tabungan Negara (BTN)'s plan to issue bonds valued at RP 750 billion (USD 79 million) in April 2005. On March 8, Bank Mega announced RP 600 billion (USD 65 million) of bonds to be issued in June. Also on March 8, Bank Danamon Indonesia said it will issue RP 2.5 trillion (USD 263 million) of bonds in April to expand its lending capacity. According to a March 9 announcement, Bank Niaga plans to sell USD 100 million worth of bonds in April and list on the Singapore Stock Exchange. BI also approved Bank Internasional Indonesia's (BII) plan to issue subordinated bonds worth USD 150 million.

On March 16, Krakatau Steel, Indonesia's largest steel maker, announced an auction of USD 100 million in bonds for the third quarter of 2005, in addition to a USD 120 million IPO planned for 2008. Indofood Sukses Makmur (Indofood), Indonesia's largest instant noodle maker, announced that it expects its net profit this year to return to its 2003 level of RP 600 billion if British courts approve the company's plan to buy back a total of USD 310 million worth of Eurobonds.

BI issued a regulation in February 2005 designed to limit commercial bank purchases of sub-investment grade corporate bonds. Effective February 1, BI ruled that commercial banks which purchase corporate bonds rated one notch below BBB minus on Standard and Poor's or Fitch Rating Agencies' scale, must be classified as substandard and have a capital provision of 15%. Bonds two notches below will require a 100% capital provision.

BI Credit Bureau

BI staff continued to work toward establishing a credit information center that will reduce credit risk by consolidating and reporting data on approximately one million borrowers. More than 2,400 commercial bank offices have registered for the service. BI plans to make available data on borrowers with loans of more than Rp 50 million (\$5,400), and projects the credit bureau will eventually include data on 20 million borrowers.

Stock Market Update

Domestic participation in Jakarta Stock Exchange (JSX) trading increased significantly in recent months, rising to 64.0% of total market transactions by value. Industry data also show a rapid increase in investment by domestic institutional funds, from RP 3 trillion (USD 315 million) in August 2004 to RP 7.7 trillion (USD 809 million) in January 2005, representing 1.1% of current market capitalization. Analysts expect continued strong participation by these funds in 2005. Market liquidity has routinely passed the USD 100 million mark in recent months. Analysts suggest the robust stock market activities are due to several factors including improved ratings of

local banks, a robust regional market, and Indonesia's stronger than expected cyclical recovery. Many listed companies are also showing stronger balance sheets.

BCA Divestment Postponed

On March 23, the GOI's Asset Management Company (PPA) cancelled plans to divest the Government's 5.02% stake in Bank Centra Asia (BCA), citing negative market sentiment. PPA hopes to sell GOI stakes in BII, Niaga, and Danamon in 2005. The PPA will seek Parliament's approval to sell government shares in two other banks in 2005, Permata (26.17%) and Lippo (1.5%).

Philip Morris Acquires 40% of Sampoerna

In Indonesia's largest acquisition in years, Philip Morris International acquired a 40% stake in clove cigarette manufacturer Sampoerna TBK on March 14. The transaction was valued at Rp 18.6 trillion (USD 1.9 billion). Philip Morris hopes to acquire the remaining 60% stake in a subsequent tender offer, tentatively within 90 days. The acquisition cost of a 100% stake in Sampoerna is estimated at RP 48 trillion (USD 5.2 billion), including the assumption of debt of approximately RP 1.5 trillion (USD 160 million). HM Sampoerna stock is the second largest on the Jakarta Stock exchange in terms of market capitalization.

Sampoerna is Indonesia's second largest cigarette manufacturer in terms of market share. The chart below highlights the financial performance of major Indonesian cigarette manufacturers, including Sampoerna, as well the company's principal non-cigarette businesses.

As of September 2004	HM Sampoerna	Gudang Garam	Bentoel	BAT
Total assets (Rp tr)	6.18	6.40		7.32
Current assets (Rp tr)	0.89	1.04		1.43
Equity (Rp tr)	9,018			9,165
		9,290		
Operating revenue (Rp tr)	7.41	7.43		7.42
EPS (Rp)	25.51	26.35		26.01
Market share (%)	5.17	6.45		6.13

Other businesses owned by Sampoerna:

Company	Industry	Ownership (%)
Taman Dayu	Property	99.0
Sampoerna Air Nusantara	Transport	99.0
Citra Investasi Nusa	Trade	97.5
Golf Taman Dayu	Sports	92.7
Sampoerna Printpack	Printing	80.0
Sumber Alfaria Trijaya	Retail	70.0

Source: Media, Analysts Data

Vice President Jusuf Kalla stated on March 22 that the GOI would gradually increase cigarette excise tax rates in 2005. Indonesia's current tax (33% of average retail price) is viewed as too low compared to that of developed countries (75%). Indonesia is not party to the Framework Convention on Tobacco Control (FCTC) signed by 168 nations.

BPK Submits 2004 Findings

On March 15, the Supreme Audit Board (BPK) submitted its findings for the second half of 2004 to Parliament. BPK found 2,128 irregularities amounting to RP 7.12 trillion (USD 748 million). BPK Chairman Anwar Nasution said that RP 5.33 trillion (USD 560 million), or 1.9% of the evaluated items were irregular due to inefficiency and ineffectiveness. The total amount of irregularities in state finances for the last five years reached RP 322 trillion (USD 34 billion). BPK forwarded two cases involving the Ministry of Defense and Indonesian Army (TNI-AD), and the Ministry of Culture and Tourism to the Supreme Court for further investigation. BPK also found irregularities in state-owned enterprises (SOEs) amounted to RP 3.8 trillion (USD 400 million) in the 2003 budget year. The average annual value of irregularities in SOEs is Rp 40.75 trillion (USD 4.3 billion). Law No. 15/2004 gives the Parliament the right to take appropriate action in response to a BPK audit.

Anti-Money Laundering Update

Indonesia's Financial Intelligence Unit (PPATK) reported that, as of March 14, it has received 1,549 suspicious transaction reports (STRs) from 80 banks and 18 reports from 13 non-bank institutions. Based on its analysis of these transactions, the PPATK said it has submitted 265 cases to the police for investigation, including 196 cases of suspected money laundering. The PPATK has also received over one million cash transaction reports from 119 financial institutions.

The PPATK signed Memoranda of Understanding (MOUs) with Belgium on February 1 and Italy on February 17. Under the MOUs, Indonesia agreed to cooperate

with the financial intelligence units of the two countries and share information in an effort to curb money laundering. Indonesia has similar agreements with the Philippines, Australia, and Thailand.

Selected Economic, Monetary & Financial Statistics

	Dec 04	Jan 05	Feb 05	Mar 05
CPI Inflation (YoY)	6.40	7.32	7.15	8.81
CPI Inflation (MoM)	1.04	1.43	1.26	1.91
Rp/USD Exchange rate ¹	9,380	9,155	9,265	9,510
30-day SBI Interest Rate ²	7.43	7.42	7.42	7.44
Foreign reserves ³	26.35	26.01	36.54	36.03
JSX Composite Index	1000	1045	1073	1080
JSX Trans Volume ⁴	1.99	2.55	2.02	
Exports (USD billion)	6.45	6.13	6.38	
% Change (YoY)	11.49	21.63	25.74	
Import (USD billion)	4.81	4.01	3.98	
% Change (YoY)	29.48	19.81	18.69	
Trade Balance ⁵	1.64	2.12	2.40	

Source: Bank Indonesia, BPS

(1) Rp/USD, end of period

(2) End of period

(3) USD billions, end of period

(4) Jakarta Stock Exchange average daily transaction volume, in billions of shares

(5) USD billions

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